Supreme Court, U.S.
FILED
OCT 29 1993
OFFICE OF THE CLERK

No. 93-541

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

NCR CORPORATION,
Petitioner,

v.

TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO,
Respondent.

On Petition for Writ of Certiorari to the Court of Appeals of New Mexico

BRIEF OF THE COMMITTEE ON STATE TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

KENDALL L. HOUHGTON
Counsel of Record
WILLIAM D. PELTZ
ELIZABETH C. BURTON
Chair and Vice-Chair,
Lawyers' Coordinating
Subcommittee
COMMITTEE ON STATE TAXATION
122 C Street, N.W.
Suite 330
Washington, D.C. 20001
(202) 484-8103

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

BEST AVAILABLE COPY

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
INTRODUCTORY STATEMENT	1
INTEREST OF *AMICUS CURIAE*	1
SUMMARY OF ARGUMENT	2
ARGUMENT	4
I. THE PRESENT CASE IS DISTINGUISHABLE FROM *CONTAINER CORP.* AND CONTROLLED BY *JAPAN LINE*	4
II. THE "GROSS DISTORTION" TEST, UPON WHICH THE STATE RESTED ITS CONCLUSION THAT FACTOR REPRESENTATION IS NOT CONSTITUTIONALLY MANDATED, CANNOT APPLY WHERE THERE IS AN ABANDONMENT OF THE PRINCIPLES OF THE APPORTIONMENT FORMULA ADOPTED BY THE STATE	7
III. NEW MEXICO AND OTHER STATES MUST BE COMPELLED TO ACKNOWLEDGE AND TO COMPLY WITH FOREIGN COMMERCE AND DUE PROCESS PRINCIPLES THAT HAVE LONG BEEN SETTLED	8
CONCLUSION	9

TABLE OF AUTHORITIES

Cases: Page

Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977) 4, 5
Container Corporation of America v. Franchise Tax Board, 463 U.S. 159 (1983) 2, 5, 6, 7
Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123 (1931) 7
Homart Development Co. v. Norberg, 529 A.2d 115 (R.I. 1987) 8
Japan Line Ltd. v. County of Los Angeles, 441 U.S. 434 (1979) 2, 4, 5, 6
Mobil Oil Co. v. Commissioner of Taxes, 445 U.S. 425 (1980) 2, 4
Moorman Manufacturing Co. v. Bair, 437 U.S. 267 (1978) 7
Tambrands, Inc. v. State Tax Assessor, 595 A.2d 1039 (Me. 1991) 8

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

No. 93-541

NCR CORPORATION,

Petitioner,

v.

TAXATION AND REVENUE DEPARTMENT OF THE STATE OF NEW MEXICO,

Respondent.

On Petition for Writ of Certiorari to the Court of Appeals of New Mexico

---

BRIEF OF THE COMMITTEE ON STATE TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTRODUCTORY STATEMENT

This brief is submitted by the Committee on State Taxation as *amicus curiae* in support of the petitioner in the above-captioned matter. Written consents of the petitioner and respondent have been obtained and filed with the Clerk of the Court.

INTEREST OF *AMICUS CURIAE*

The Committee on State Taxation ("COST") is a nonprofit association that was organized in 1969 as an advisory committee to the Council of State Chambers of Commerce. COST, which was separately incorporated on January 1, 1992, has a membership of more than 400 major multistate corporations, engaged in interstate and international business. COST's objective is to preserve

and promote equitable and non-discriminatory state and local taxation of multijurisdictional business entities.

Many of COST's member companies are engaged in business in the State of New Mexico, and most if not all are engaged in business in at least one state which employs the New Mexico method of taxing foreign source income of domestic corporations. That is, the states include foreign-source income in the domestic parent's apportionable income without inclusion in the parent's apportionment factors of any amounts representing the income-producing factors of the foreign subsidiary-payor. At the same time, these COST member companies are subject to a direct, unapportioned tax on their foreign-source income by the foreign jurisdictions in which the income is earned. Therefore, COST has an interest in the instant case.

SUMMARY OF ARGUMENT

In previous cases, this Court has set out some clear-cut general rules by which an apportionment formula should be judged. The case of *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159 (1983), adopted an external consistency rule that was first contemplated in Justice Stevens' discussion of factor representation in *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980) (Stevens, J., dissenting). Factor representation provides that if value is included in an apportionable tax base, the quantities that generated such value must be included in the apportionment factors. Where, as in this case, the payroll, property and sales included in the factors do *not* correspond with the income subject to formulary apportionment, the formula used cannot be sustained under the authority of *Container Corp.* The case of *Japan Line Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979), established the rules by which to determine the constitutional sufficiency of a formula used to apportion income generated by foreign commerce. It set out that where, as in this case, there is inevitable international

multiple taxation of such income, there is a violation of the Foreign Commerce Clause.

The state cannot take refuge in the axiom that, even though distortions are produced by a facially arbitrary formula, it did not miss by much and so is tolerably inaccurate. However useful the test of distortion may be in comparing one apportionment formula to another (*e.g.*, the one-factor versus three-factor formula), it is of no use where the formula is agreed upon but where the principles of that formula have been abandoned. Here, the three-factor formula is agreed upon, but the state has abandoned the fundamental principle of that formula, *i.e.*, that payroll, property and sales that generate income should be used to apportion that income. The state's clear failure to follow the principles of the formula it has adopted should not be condoned, where the error is obvious (the denial of meaningful factor representation) and the corrective measure is equally obvious (factor representation).

While some states use the tools provided by this Court to determine the constitutional sufficiency of an apportionment scheme, others have been unwilling to do so. This Court should ensure that when states exercise the broad discretion that they are accorded to choose an apportionment formula, they do so in a principled manner.

ARGUMENT

I. THE PRESENT CASE IS DISTINGUISHABLE FROM *CONTAINER CORP.* AND CONTROLLED BY *JAPAN LINE.*

Three cases decided by this Court within the last 15 years set forth the principles that guide analysis of the issues in this case. In *Mobil Oil Corp. v. Commissioner of Taxes,* 445 U.S. 425, 441 n.15 (1980), this Court acknowledged the issue whether factor representation is required either (i) as an established element of all apportionment schemes, or (ii) as a remedial measure where a particular apportionment scheme results in inevitable international multiple taxation. Although the Court declined to resolve the question in *Mobil* on grounds that it was not timely raised, 445 U.S. at 441 n.15 and at 449, Justice Stevens both analyzed and answered this critical question in his dissent, where he stated:

> Unless the sales, payroll, and property values connected with the production of income by the payor corporations are added back to the denominator of the apportionment formula, the inclusion of earnings attributable to those corporations in the apportionable tax base will inevitably cause [the payee's in-state] income to be overstated.

Id. at 461 (Stevens, J., dissenting).

In *Japan Line Ltd. v. County of Los Angeles,* 441 U.S. 434 (1979), this Court established the principle that in the context of foreign commerce, a state tax must satisfy two distinct Foreign Commerce Clause tests in addition to the four universally applicable Commerce Clause tests articulated in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977).[1] The two considerations distinct to

---

[1] In *Complete Auto,* this Court resolved a Commerce Clause challenge to a tax by analyzing whether such tax "is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce,

taxes impacting foreign commerce are: (i) whether, notwithstanding apportionment, the state tax creates a "substantial risk of international multiple taxation," and (ii) whether the state tax will "impair federal uniformity in an area where federal uniformity is essential," by preventing the federal government from " 'speaking with one voice when regulating commercial relations with foreign governments.' " *Japan Line*, 441 U.S. at 451.

Container Corporation of America v. Franchise Tax Board, 463 U.S. 159 (1983), embodied the *Mobil* principle in its statement of the "external consistency" rule. An apportionment formula under both the Due Process and Commerce Clauses must be fair, and one test of fairness is the external consistency test, *i.e.*, "the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Container Corp.*, 463 U.S. at 169. The formula at issue in *Container Corp.* was deemed fair because it incorporated factor representation into the apportionment of foreign-source income;[2] but New Mexico's formula is *not* fair, because it does not allow such representation. Further, this Court in *Container Corp.* applied the principle set forth in *Japan Line*, and found that the formula under review did not cause inevitable international multiple taxation.

The Court of Appeals of New Mexico relied on *Container Corp.* in deciding this case, *see* Petition, App. A at 9a. However, the holding of *Container Corp.* is distinguishable from the present case, precisely because the taxpayer therein was allowed to include in the apportion-

---

and is fairly related to the services provided by the State." *Complete Auto*, 430 U.S. at 279.

[2] Because California utilized the unitary combination method of apportionment, it included the income-generating factors of each corporation in the unitary group in the denominators of the apportionment formula.

ment formula the payroll, property and sales that generated the foreign income. In this case, NCR has never been allowed factor representation. *See* Petition, pp. 8, 12. Because the formula at issue in *Container Corp.* fulfilled the requirement of factor representation, its holding cannot be extended to support the New Mexico Court of Appeals' decision in this case.

In addition, the refusal to permit NCR to include in its factors the amounts of payroll, property and sales that generated income from which dividends, royalties and interest were paid means that its foreign-source income will suffer inevitable international multiple taxation. The double income tax burden in this case is no less real and no less inevitable than the double property tax burden on the containers under consideration in *Japan Line*. *See* Petition, pp. 12-13 and nn.7 and 8 thereto. This Court's decision in *Japan Line* established the principle that inevitable international multiple taxation is in *every* instance prohibited. Because this standard is not limited by the factual considerations in that case, *Japan Line* is controlling and the distinctions drawn by New Mexico between NCR's case and *Japan Line,* based on the type of tax and taxpayer involved, are invalid. There is no room for equivocation with respect to this standard; once inevitable international multiple taxation is established, the fifth prong of the Foreign Commerce Clause test is violated. *See Japan Line,* 441 U.S. at 446; *Container Corp.,* 463 U.S. at 185-186. This problem could be corrected simply by giving representation in the apportionment formula to the payroll, property and sales that generated the apportionable income.

II. THE "GROSS DISTORTION" TEST, UPON WHICH THE STATE COURT RESTED ITS CONCLUSION THAT FACTOR REPRESENTATION IS NOT CONSTITUTIONALLY MANDATED, CANNOT APPLY WHERE THERE IS AN ABANDONMENT OF THE PRINCIPLES OF THE APPORTIONMENT FORMULA ADOPTED BY THE STATE.

In determining the constitutionality of one apportionment formula as opposed to another, this Court has established very liberal standards. In the case of *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931) (one-factor formula versus separate accounting), this Court held that a formula that operated "so as to reach profits which are in no just sense attributable to transactions within its jurisdiction" (p. 134) violated the fair apportionment requirement of the Due Process and Commerce Clauses. On the other hand, this Court has declined to strike down apportionment formulas that " 'may result in taxation of some income that did not have its source in the taxing State. . . .' " *Container Corp.*, 463 U.S. at 169-170 (three-factor versus separate accounting) (citing *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267, 272 (1978) (one-factor versus three-factor)). In the context of a challenge to one apportionment formula grounded in a taxpayer's preference for another formula, this Court has declared that the taxpayer must prove either (i) that the challenged formula attributes income to the taxing state that is " 'out of all appropriate proportions to the business transacted . . . in that State,' " or (ii) that it has " 'led to a grossly distorted result.' " *Id.* at 170.

However, the distortion standard has no role in the constitutional analysis where the formula is agreed on but its principles are abandoned. The State of New Mexico seeks to use the form of the three-factor formula, and your *amicus* does not understand NCR to object to that. But New Mexico has ignored or abandoned the principles on which the formula is based. The State chose

an apportionment formula widely used because the three factors in combination "reflect a very large share of the activities by which value is generated," *id.* at 183. It then included value (income) in the tax base to be apportioned, while arbitrarily refusing to recognize the factors that generated that income. This is not a case where the taxpayer seeks to use a different formula. Here the taxpayer seeks adherence to the principles of the formula chosen by the state; so there is no need to resort to some standard of distortion to determine whether correction is required.

III. NEW MEXICO AND OTHER STATES MUST BE COMPELLED TO ACKNOWLEDGE AND TO COMPLY WITH FOREIGN COMMERCE AND DUE PROCESS PRINCIPLES THAT HAVE LONG BEEN SETTLED.

COST's members and other multinational corporations have been subjected to a miscellany of erroneous interpretations of the constitutional precepts that pertain to the question of factor representation. They often must expend tremendous resources in struggles with states, including New Mexico, to define the general spectrum of what is permitted or required in each state's apportionment scheme. This Court has established working principles such as inevitable multiple taxation and internal and external consistency to guide the determination whether an apportionment scheme is unconstitutional in its design and/or operation. In the use of these principles, the states sometimes succeed in enforcing the integrity of an apportionment fomula. *See, e.g., Tambrands, Inc. v. State Tax Assessor*, 595 A.2d 1039 (Me. 1991) (factor representation required when income received from foreign subsidiaries is included in taxpayer's apportionable base); *Homart Dev. Co. v. Norberg*, 529 A.2d 115 (R.I. 1987) (required inclusion of partnership's factors in apportionment formula of nondomiciliary corporation that held interest in and received income from the partnership). But

often, states attempt, as New Mexico has in this case, to avoid the use of these rules by resorting to artificial factual distinctions and analytical subterfuge, in a bid to enforce apportionment schemes already demonstrated to be unconstitutional. This Court should enforce the application of its own announced rules to the case at hand.

CONCLUSION

For the reasons set forth above, the Committee on State Taxation respectfully requests that petitioner's petition for writ of certiorari be granted.

Respectfully submitted,

KENDALL L. HOUHGTON
Counsel of Record
WILLIAM D. PELTZ
ELIZABETH C. BURTON
Chair and Vice-Chair,
Lawyers' Coordinating
Subcommittee
COMMITTEE ON STATE TAXATION
122 C Street, N.W.
Suite 330
Washington, D.C. 20001
(202) 484-8103

Dated: October 29, 1993.